0:04
Nigel Coe: Thanks, everyone, and good afternoon.

0:07
My name is Nigel Coe, from Wolfe Research. I'm the firms' Multi-Industry analyst and thanks for joining us for the conference. As we get into the, as you say, in baseball, bottom of the ninth innings here, on the third day of the conference, delighted to be welcoming General Electric to the to the podium. And I'm joined by GE CFO, Carolina Dybeck Happe. Carolina, thank you very much for being here. It's a pleasure. Carolina, I think you're going to make five minutes of opening remarks or so, and then we'll get into Q&A. So Carolina over to you. Thanks.

0:42
Carolina Dybeck Happe: Hi Nigel and thanks for having me. It's great to be here with you. And I'm still working on learning those baseball terms, but I'm getting there. I'm in the best city in the world for that. It's help in Boston and moving.

0:55
Well, we're more than halfway through the second quarter, and it's been exciting, and busy. We've held our quarterly operating reviews, with each of the businesses, and I'm really encouraged by the progress that we're seeing at Power, especially in Gas Power services. At Renewables, we're very focused on building a profitable growth business, and we continue to see strength in Healthcare. Aviation is still our most challenged market. We're planning for some recovering the second half, and I'll speak to this in more detail shortly.

1:29
But, first, I'd like to share some insights on our transformation and our recent leverage actions. Now, our journey to become a more focused, simpler, and stronger industrial company is accelerating. And with the AerCap-GECAS combination announced in March, we're focusing on our core Industrial businesses, capturing opportunities presented by the future of light, precision health, and the energy transition. And upon close with AerCap, it will drastically simplify our reporting structure, going from three columns to one column financials. And it will serve as another catalyst to significantly reduce debt by more than $70 billion over 3 years.

2:13
And, given our stronger financial footing, we've executed additional actions this past week. First, as the next step in our deleveraging plan, we announced a balance tender of short and long duration debt. Due to our strong liquidity position, we acted opportunistically, funding this with cash on hand. And we're continuing to evaluate future deleveraging opportunities, and they're based on economics, deleveraging impact, risk mitigation and optimal capital structure. And today, we also closed on the refinancing of our backup credit facility. Due to our improved liquidity position and lower cash needs, we reduced the size to $10 billion from $15 billion and we extended the maturity date from 2023 to 2026 at attractive pricing. And overall, we remain committed to achieving a less than 2.5 times net debt to EBITDA over the next years, thanks to our finance teams who continue to be instrumental in making this happen.

3:13
At the same time, we've been fortifying our foundation. And our learn progress is key. As we scale lean, we're working to improve Safety, Quality, Delivery and Cost - SQDC - in that order, fueling high quality growth. And lean, coupled with our significant decentralization effort is

enabling this work and maximizing impact where it matters - closest to the customer. Of the businesses I wanted to touch on, now Aviation.

3:45
So in Aviation, we are seeing some regional differences in the market recovery. So what does that mean today? Broadly speaking, GE and CFM departures are up just slightly in May and April vs. March, although some of the positive momentum we saw in April has tempered in May. We're monitoring customer behavior in addition to the vaccine rollout and global border restrictions - both remain uneven. Some additional regional callouts. China is nearly back to 2019 levels with rising load factors. APAC, ex China, continues to lag. This region has the largest proportion of total border closures, compared to other regions, and is being impacted by the tragic COVID situation in India. North America carriers are cautiously optimistic with increasing travel confidence, and some carriers are vocal about adding capacity for the upcoming summer season on domestic routes. Europe significantly lagging down roughly 75% vs. 2019 levels, we will see what happens. And Latin America, it's a tougher story in light of the recent rise in COVID cases. Just for context, pre-COVID more than 60% of the GE and CFM departures were concentrated in North America, Europe, and China. So near term, we expect we will be more impacted based on the recovery timing in these regions, and we're monitoring global trends across our customer base.

5:22
So, stepping back, we're planning for some recovery in the second half. Our Aviation business has the largest and youngest engine platforms, and we have more than 37,000 commercial engines installed, and more than 60% of our fleet has not yet had the second shop visit. And just last week we announced an agreement with indigo to power 310 new aircrafts with out CFM LEAP-1A engines. The agreement, one of the largest in CFM's history, includes 620 new installed engines and associated spare energies, plus of course a multi-year service agreement. Overall, our platform is well positioned to generate value for decades to come.

6:06
In summary, we had a solid start to the year, and we're set up to deliver on the 2021 commitments we shared with you in March. Across all of our business, services remain a core strength. Despite some near-term pressures, services orders were up 6% organically in the first quarter, excluding Aviation. And longer term, with half of our revenue in services, this represents a tremendous growth opportunity. Reflecting on my last year with GE, I'm very happy to be part of the team at this really critical point in our transformation. So thank you for letting me share those thoughts, Nigel and over to you.

6:45
Nigel Coe: Great, thanks, Carolina. You mentioned the last year, and you're very happy to be at GE. And I'd be curious, you know, what's changed in that year and what transformation is being made to the finance function, you know, as you go, from three columns down to one column?

7:03
Carolina Dybeck Happe: Yeah. So now, I'm just sort of realizing that the last year, it's actually my first year, right? And I would say that it was probably hard, too imagine a more challenging environment to begin as CFO of GE, just because a COIVD. What I would say though is that, in during this year we've taken a number of important steps, and our efforts to strengthen the balance sheet, were obviously paramount. And by that, I mean all the efforts we've put in to

reduce the debt, I spoke about the $70 billion reduction, but also simplifying our portfolio - Biopharma, Baker, Lighting, and now the AerCap transition. And beyond balance sheet and portfolio, we're also setting up the company for a strong rebound following the pandemic. And I would say, we took advantage of the urgency that was created out of COVID; good companies act fast, right, so we acted fast and with that we accelerated GE's transformation.

8:08
And what do I mean by that? Well it's really about, what I would say, it includes adopting lean in the way we operate and how we go forward. And that's all supporting our restructuring with sustainable cost out actions that I've talked about previously. On the organization, how it's changing, I would just start by saying I'm really impressed by the people I've met and I'm so grateful to have the opportunity to lead this really talented team. And there are many things we do, and I would say in the spirit of lean, we do a lot of things well, but we can do a lot of things even better - and that goes for finance as well. And I would say, you asked sort of what I'm thinking or how am I shaping the function as well? So, I would say first of all, in finance we have a strategy to help GE to drive GE's transformation and part of that is really making sure that we look at the company with a deeper operational visibility, and a greater focus on cash. So I would say we're working on getting the right data, at the right level and the right frequency to our business leaders so that together we can drive the right and the most important decisions with speed.

9:22
So, when I looked at that, I said, ok, first, right data to be able to take decisions, and we have focused on a more operational, more granular P&L. We've also updated the working capital definition that we've shared with you, so that it's better aligned with how we really run the company and how we can drive improvements. The right data is one thing, but also the right frequency, faster, more frequent. You talk about broadly implementing monthly close, weekly collections, and I would call, say that's our road to daily management.

9:53
The third one is, on our journey to more decentralized company, I'll admit being one of the drivers behind us having almost 30 P&Ls now, into this year in our five segments. So that's also an important enabler to make sure that we have them at all the right levels. I would say today, I'm proud to say that every finance employee in GE is working on some of those priorities.

10:21
Nigel Coe: All right. So you talked about taking down the revolving credit facility down to $10 billion. I can't remember what it was two years ago, it was certainly north of $30 billion. Factoring is down to, I think by the end of this quarter down to about $3 billion. Is that a signal of this improved cash management and consistency of cashflow from the businesses?

10:48
Carolina Dybeck Happe: Yes, definitely. When we talk about cash management have talked about linearity because it's about improving the linearity and we talk about cash management and improving cash linearity, rather, reducing the nonlinearity. What that does is, and also now going into the fact that we don't do factoring anymore, so basically you're looking at how do I generate cash on a more linear basis, which means earlier on in the quarter. So to do that I obviously need to collect faster. So, how do I do that? Well, I need to improve collections from, well much more frequently. I also need to bill more frequently, and earlier on in the quarters, right. So also billing

is earlier on in the quarter. Frankly what we don't talk about is also, well we do talk about it, but not quantifying it here is that, billing earlier means that you're delivering earlier. So, it also helps operations and the way that we have a much more smoother profile in how we deliver to our customers. So basically, happier customers, but also better free cash flow profile for us in a much more smooth way.

11:55
Nigel Coe: That's great. So speaking of linearity of free cash flow, can we talk about maybe second quarter free cash flow? You talked about it being better year over year. Low bar because you had a $2 billion cash burn in the prior year quarter. Normally, second quarter is stronger than first quarter. I just wanted to hear any kind of context on second quarter, and it's moving pieces, you see.

12:22
Carolina Dybeck Happe: So for the second quarter, specifically, I would start by saying, yes, we still expect it to be negative, but we do expect a similar level of improvement as we saw in the first quarter, which we talked about was about $1.7 billion. What I also see though is that in the second quarter, we will be sequentially pressured by some of the tax payments, we pay tax in the second quarter this year compared to third last year, but also some timing of AD&A. I could also see the big reduction of factoring not being 100% smooth, even if it's only a timing matter. And if I look at the year-over-year specifics, and if you take the second quarter, obviously the improvement will be driven by better cash earnings - combination of the cost out actions, as well as the growth the way we expect, especially in Healthcare, PDx was very hit last year, and now it's coming back, so that's going to be a positive. And also, I expect to see working capital continue to improve, both continue to improve underlying processes then we also have the, I would say, the specifics of last year, where we had a big accounts payable pressure last year, which we don't expect to repeat this year. On the other hand, we also had Military progress as a positive last year that we don't expect to see this year. And then the last one, I think I mentioned that one, was on the AD&A which I expect to be worse this year. In a way, good of course since it means that our customers are delivering overall.

14:00
Nigel Coe: And the factoring to work down, I think you've said the bulk of that will be done this quarter. Is that still on track to be done by the end of this quarter?

14:11
Carolina Dybeck Happe: Yes.

14:12
Nigel Coe: Ok, so no confusion around free cash flow in the back half of the year, should be very clean - what you see is what you get, basically. Ok good. Any additional comments on the second half free cash flow coming out or should we just move on to longer term free cash flow?

14:25
Carolina Dybeck Happe: On the second half, we expect continued improvements in earnings and working capital. There are a couple of specifics though that basically second half last year that I would like to call out in that case. Remember we talked about the Boeing 737MAX payments, it's about $0.5 billion headwind, and we also had at the end of last year significant progress payments from large, bulky Renewables orders that we know are lumpy by nature. And then

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there was also an impact from the deferred payroll taxes with the Cares act that you don't see this year.

15:02

Nigel Coe: Ok, great. So the high single digit margin, $7 billion or so of free cash flow, you know, your targets. Maybe talk about some of the major moving pieces behind that. What do you see as the major driving forces, outside of earnings, to get to that level of free cash flow? And maybe talk about how you see the businesses within that mix.

15:28

Carolina Dybeck Happe: Yeah, sure. We've talked about the high single digit margins, right, and we've talked about 2023 plus, which basically would imply a $7 billion plus free cash flow on the base of 2019 sales. I would say though, you talked about what's outside of earnings, but the growth will come primarily from earnings. And I see that as being sort of critical to enforce that it's really based on healthy organic growth, focuses on services makes continued operational improvement, and then lean and the work we're doing will help offset some of the natural working capital needs that we would have with growth. And then, on top of that, we also expect to spend significantly less on restructuring, legal and pension. And that's, you know, up to a couple of billion compared to 2020.

16:21

You asked about it per business. So, why don't I take it business by business then. Starting with Aviation. We have talked about that we expect the commercial markets to recover to 2019 levels, and that we continue to work on the cost out and that we expect to see high single digit revenue growth in Military, despite this year’s challenges. This would then translate to free cash flow also at the levels that we saw in 2019, so basically more than $4 billion, and we can see sort of a conversion rate of more than 90%. We've also talked about that cash will recover faster than at op profit. I would say partly because as we continue to have the portfolio transition with the introduction of new engines, it gets a negative mix. Then over time we expect the margins to return to high teens and that would basically give you an op profit of more than $6 billion from Aviation.

17:24

In Healthcare, it's very much about growth. So here it's about continuing to invest in the profitable growth, and we talk about new, exciting products, right. Balanced with that we of course continue with lean here as well, so we continue to take cost out, but also to improve working capital. And here we're planning for continued low-to-mid single digit revenue growth, and the annual 25 to 75 bps of margin expansion. And I would say the normalized cash flow conversion here will be around 100%. This would get you to $3 billion to $4 billion of op profit.

18:09

For Power, we expect to see the continued improvement in Gas, and really driven by the services growth and the cost out. And, we've also talked about that we're very focused on equipment underwriting or improving our equipment underwriting, which basically means less turnkey scope and better risk return equation over time. We’re on plan to achieve high single digit margin this year in Gas Power. And we also talked about that we would expect this to be maybe 90% free cash flow conversion by 2022. The smaller businesses in Power - we're completing the restructuring of the exit of the new build coal in Steam. I would say that the combination of Steam, Power Conversion, and Nuclear, we expect both profitable and generating cash in 2023.

19:07
And then Renewables, here we expect a profitable growth in Onshore Wind, both through services growth and cost outs. And, as we start to see revenue growth from Haliade-X, revenue and bottom line, in Offshore Wind, that's also going to drive margin expansion and cash. Then we have our turnaround of Grid, which continues. I would say, overall for Renewables, expect the business to have positive free cash flow this year and to be breakeven by 2022, which is next year. Finally, maybe just to mention. Corporate continue to improve and to reduce costs as we move on our decentralization journey. I would also add that going forward, of course, I've talked about working capital and working capital improvement, but also, efficient capital deployment is key across the businesses. If you aggregate all of that, you basically get to our high single digit free cash flow margin target and overall cash conversion of 85-90%.

20:15
Nigel Coe: Right, perfect. So it looks like you're targeting $4 billion dollars of Aviation free cash flow, about $3 billion for Healthcare, I'd say about $1 billion also for Power and Renewables as a bucket, and perhaps $1 billion outflow corporate other items. Is that a fair framework?

20:37
Carolina Dybeck Happe: So, I gave my details and you did the math on that, so I think we're good.

20:44
Nigel Coe: Yeah, my math is not always 100%, like your free cash flow conversion. So on pension, I did want to touch on pension because you mentioned the bridge to the leverage targets and pension is basically all of your leverage at this point to a pro forma leverage. The rating agencies are using the $20 billion year-end 2020 number. Can you just bring us up to speed on terms of where we are at current discount rates, current market returns on that $20 billion today?

21:16
Carolina Dybeck Happe: I actually really appreciate the question, and I would also say that pension, so it's a topic and it's not always well understood. Maybe some, some background to us and our pension. So we've worked really hard to derisk the pension profile. And that really comes down to four areas that we talk about. So you have the design of the plans, the investments, the funding and the settlements. You start with the design. A couple of big important parts that have happened. First of all in 2019, we announced that we would freeze the US plan for salaried and reduce the benefits for the execs. Basically, that reduce the deficit by $1 billion and reduce the annual service costs. We expect that the service cost is down to about half of what it was, and basically $500 million in 2021. We've also talked about that we're also working on freezing our UK Pension Plan, but that still work in progress. So design is one important one.

21:25
The other one is really on the investments, and I would say here, we really continue to actively manage the investment portfolio and we've had 2 years of strong returns, 18% each and also realigned the fixed income portfolio with the hedge portfolio. So today about half of the risk we have in interest is hedged.

22:49
On the funding side, if I look at 2018 we put in $6 billion and at the end of last year, we put in $2.5 billion, so $8.5 billion pre-funding. And then, if I look at sort of where we are, The US Plan

has about $10 billion of deficit and we don't expect, as we talked about, we don't expect any funding through the end of the decade, and it's really a combination of the asset returns, the pre-funding, but also the American Rescue Plan Act. And then, we also have the other part, which is the “Pay as you go” plans. It's about the other $10 billion of deficits, and here we expect to see sort of standard payments of half a billion per year, which is included in our free cash flow. I think what's interesting is, when we talk about this, equal PAYG plans, I'm going to leave the valuation to you and others to do. But the way to look at it is that you either include it in the free cash flow as we do or you view it as liability, but not both cause I have seen there have been some confusion in that. You decide which one, but it's not both.

24:03
And finally, on settlements. I’ve gotten questions about so what are you doing about settlements? What are the opportunities there? And I would say, we do look at opportunities. We have maybe an opportunistic view, and I would say that they need to sort of fit both criteria - reduce deficit, but also be economically viable. So as long as that's balanced then we do changes. I'm not going to mark the pension here now, but you're right. So clearly we're benefiting from higher rates, net of the hedging impact that I talk to you about. By the end of the year, basically, the mark will include both the impacts and the asset returns. And, on the sensitivity, it still stands. So we've talked about that for every 25 bps, it's $2.4 billion of impact, but half of that is hedged. So, I would say the 25 bps is basically equivalent to a little bit above $1 billion of impact.

25:09
Nigel Coe: There's a lot of data coming in. You mentioned that, you know, you've got funding relief on the principal plan. So no funding envisaged for the foreseeable future there. And on the pay to go, I think more than half of your liability is Pay as you go and there's no funding requirements there, you’re already funding those progressively. So there's no funding call there. It feels like your pension, kind cash claims here, are very well defined, is that fair?

25:40
Carolina Dybeck Happe: Absolutely. Yeah, we're in a much better place compared to where we've been historically, so really happy about that. I'm happy about sharing the news that no funding needed for at least the decade.

25:54
Nigel Coe: Great, fantastic. In your prepared remarks, you talked about Aviation margins, you know, $6 billion of op profit, high teens margins. As we sort of ramp up the curve, with obviously Airbus talking about getting to potentially 60 to 75 build rates per month, as that OE increases what are some of the R&D funding requirements and what OE pressure might we see in the margins as we come back up that curve? Anything to call out there?

26:28
Carolina Dybeck Happe: I would just maybe start by saying that we expect to get back to 2019 departures. We've talked about narrow bodies in 2023, widebodies in 2024. And we've talked about the shop visit, for example, we don't expect them to be back to peak until beyond 2023. We are confident, though, that we'll get back to 2019 levels and that's both revenue, margin, and cash. How we get there will depend, or how fast we get there, will depend on the market recovery and the impact it has on us. I would start by saying that the shop visit revenue recovering to 2019 levels by 2023 fine, and then the margins we talked about returning to the

historical high teens, and that is including the cost actions that we did. If you talk about the R&D and the new platforms, I talked about that in my introduction remarks. So yes, we'd be a headwind as we go through sort of the portfolio transition, but I would say that's usually as volume ramps, some of the temporary cost out measures will come back and we will have the restructuring savings there but you also need to look at the mix on the new platforms. Money wise for R&D, I would say as a percentage of sales we expected to sort of continue to be on the 7-8%. That is both internal and external funding, and I would say overall, we do expect also that the third party funding will sort of continue to increase over time. But how it's actually handled is on how this plays out.

28:22
Nigel Coe: Fantastic, and then, you mentioned Power services and that's been, you know, a perennial problem child since for the last three years it's been flat to negative for most of that time. Maybe just to clarify your comments on what you're seeing right now, in Power services and maybe talk about transactional CSAs and upgrade activity.

28:45
Carolina Dybeck Happe: Yeah. So on Power margins, I would just start by saying, we're still tracking towards the high single digit margin for Gas Power and key to this is clearly the services part. We expect to see low single digit services revenue growth this year, which is the higher margins, better mix - very much service focused here. I would also say that we continue to see improvement, where we talked about different types of services as well. So you have the contractual and you have the transactional. So we expect to see good results on both. We also talked about transactional having a good backlog coming into the year. So we do expect that to be a big part of how we get Gas to high single digit margins this year.

29:44
Nigel Coe: And Power services are still your highest margin revenue stream in Power? I think we used to think of this as a 20% type margin business. Is that's still sort of a decent number?

29:57
Carolina Dybeck Happe: It’s definitely the highest part Power margins, yes.

30:01
Nigel Coe: We're running a bit short on time, but there is a question or two from the audience if I can just throw those in. One here, what's been done to ensure negative news makes its way up, the chain, senior management, unlike the past?

30:19
Carolina Dybeck Happe: I would say that something that's very sort of near and dear to my heart, and also as a company, sort of embracing reality and making sure that we have transparency and candor. And I think it's important how you treat people who come with with bad news. So now, I think that the critical thing here is really that it’s not about the news, it's about what are you going to do about it? That's the important part. And I think that people see that and they trust us and the trust the system that it's really about what are you doing to fix things? And not sort of what is the issue at hand? It's about what are you doing to improve it and focus on continuous improvement. And in that, in that environment, it's a very different environment where people then share, and they work on improving, and together we move forward.

31:11

Nigel Coe: Great. And then just one more clarification on factoring. The second quarter, I think you've talked about $5 billion of factoring reduction. Is that primarily going to hit in 2Q or is it 2Q and the second half of the year?

31:26
Carolina Dybeck Happe: So what we have set up is that a majority of the $3.5 billion to $4 billion, that is going to be part of our discontinued factoring, will be felt in 2Q.

31:35
Nigel Coe: Right. That's, that's perfectly clear. Well Carolina I can't believe half an hour, has already passed by, so thank you so much for your time. It's been a pleasure to host you for Q&A and good luck and speak to you soon.

31:47
Carolina Dybeck Happe: Absolutely, thank you for having me.

31:49
Nigel Coe: Thanks Carolina.

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